

Package 2

COMPREHENSIVE TAX REFORM PROGRAM

Corporate income tax and incentives reform

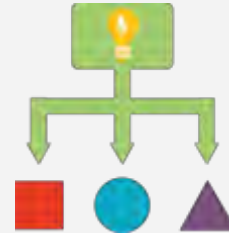
As of 2 October 2018 11:00 am

Content of Package 2 presentation

**Why is Package 2
necessary?**



Proposed reform

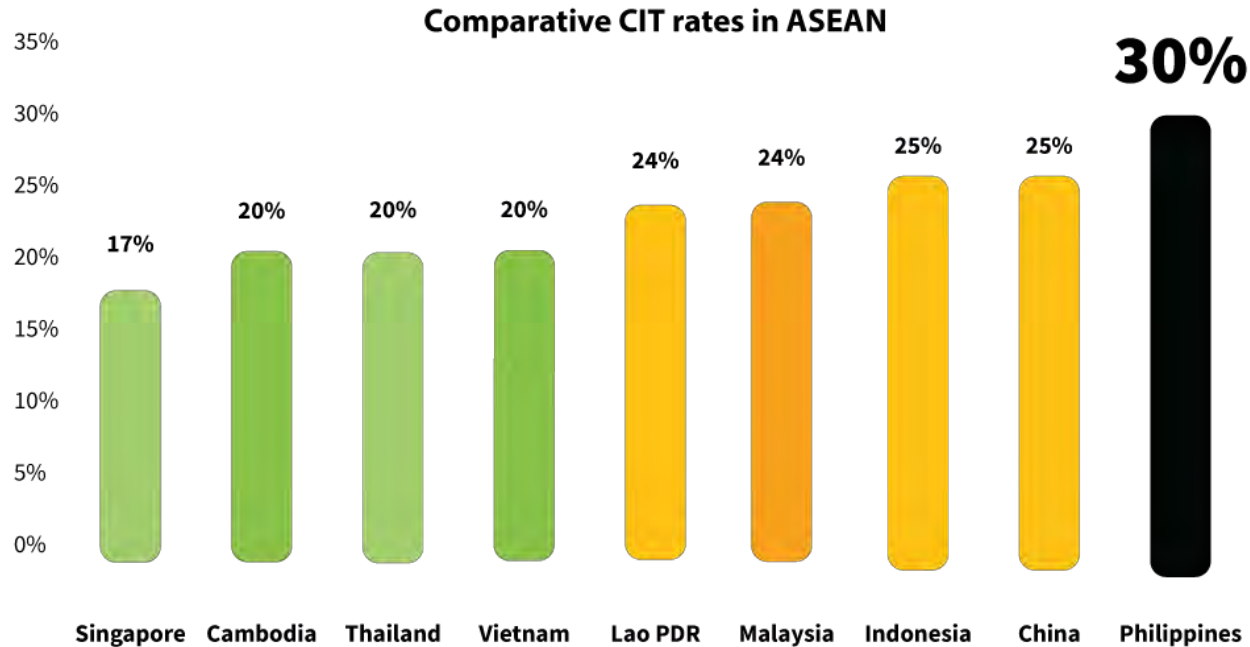


1. Broaden tax base



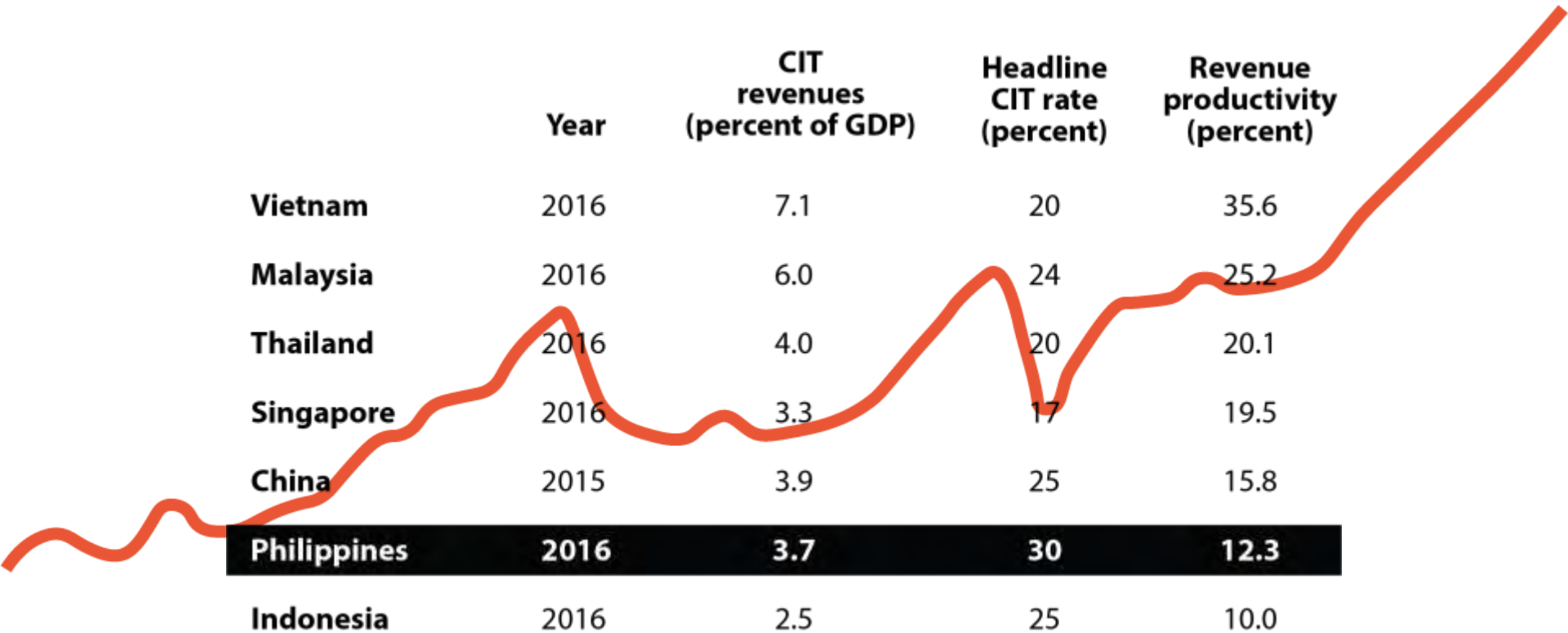
2. Simplify and make the tax system more equitable.

The Philippines has the highest corporate income tax rate in the ASEAN region.



Source: Asian Development Bank and PWC

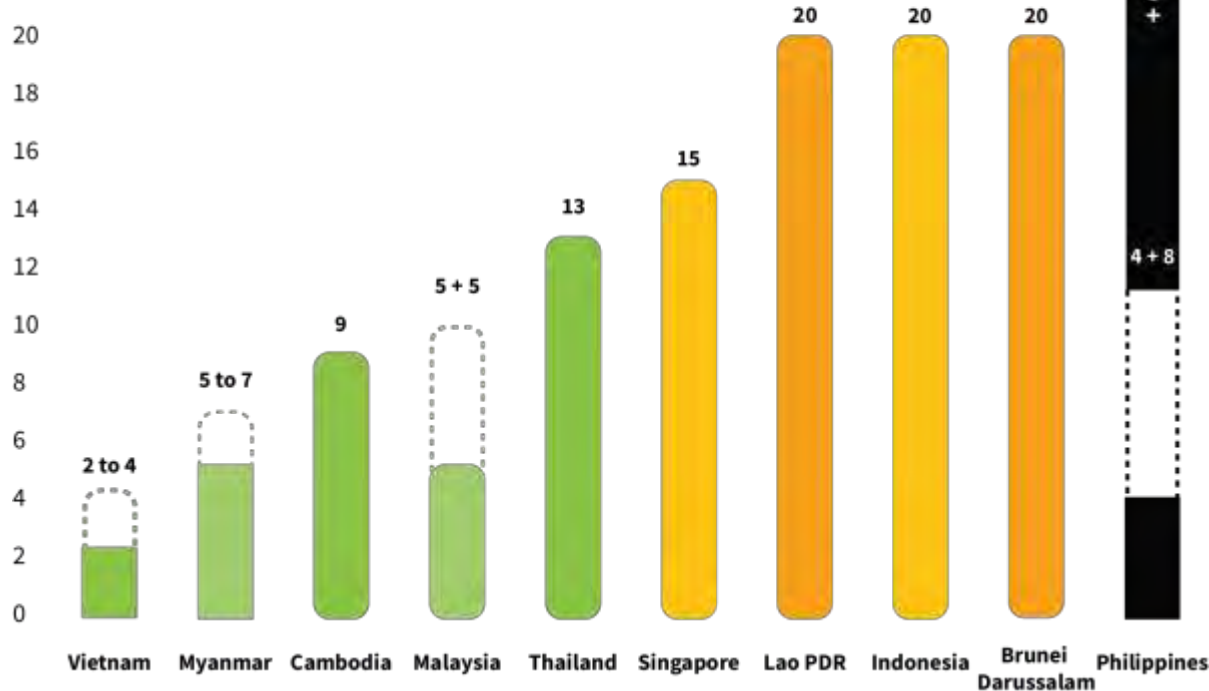
CIT revenue is increasing, but efficiency is very low.



Source: OECD, individual country statistics offices, and DOF staff calculations.

We have a complex tax incentives system.

Maximum years of income tax holidays in selected Asian countries



We grant the most generous fiscal incentives since they are in lieu of all taxes and given **forever**.

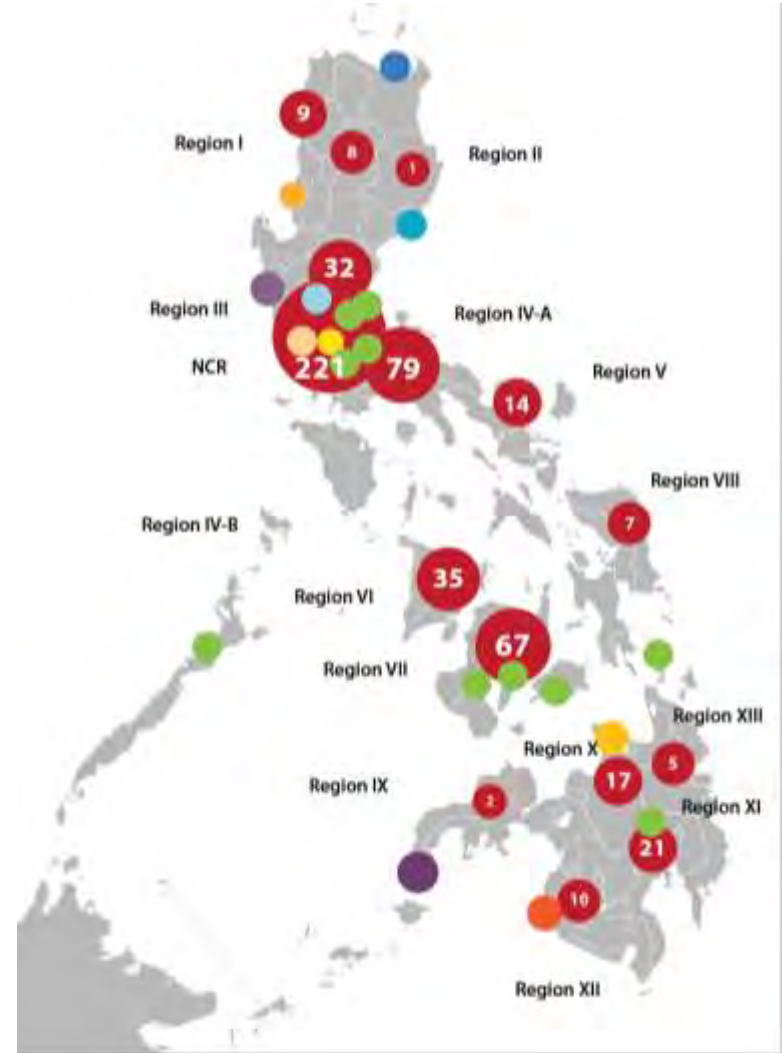
- **14 IPAs**
136 investment laws
200 non-investment laws
546 'ecozones' and freeports

Source: Individual country finance agencies and investment promotion offices.

We have a complex tax incentives system

(based on latest data available)

IPA	No. of ecozones
AFAB	1
APECO	1
BCDA	1
BOI	-
CDC	1
CEZA	1
PEZA	528
PIA	1
PPMC	1
PRA	-
TIEZA	8
SBMA	1
RBOI-ARMM	1
ZCSEZA	1
TOTAL	546



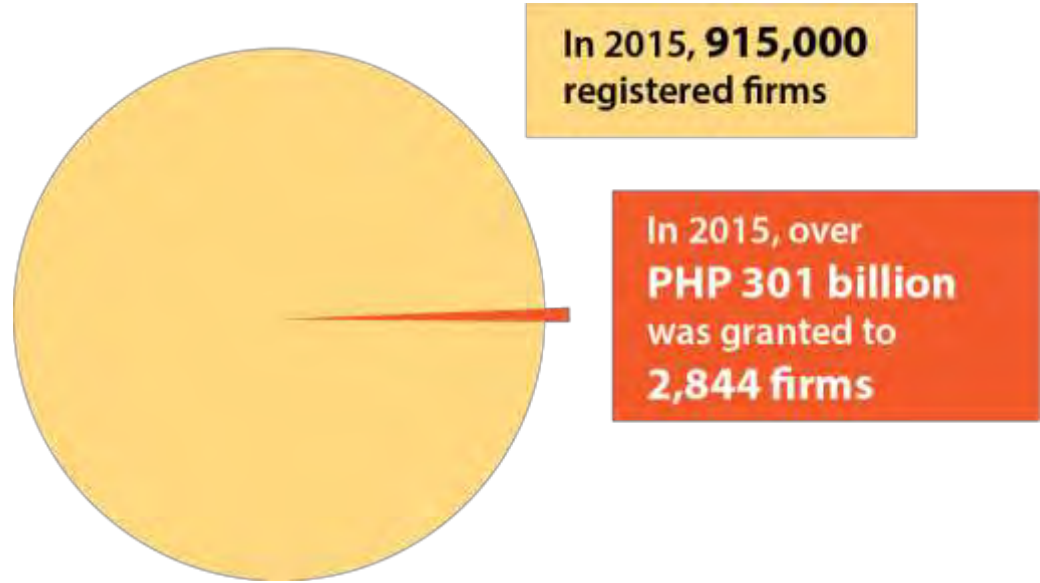
Source: PEZA, IPAs, and DOF staff calculations

Huge inequity under the current system:

Firms with no incentives pay the regular rate of 30% of net taxable income

Firms with incentives pay between 6% and 13%

For example, almost all of the 90,000 SMEs pay the regular 30% rate.



Source: DTI and TIMTA

Estimated forgone revenue due to tax incentives

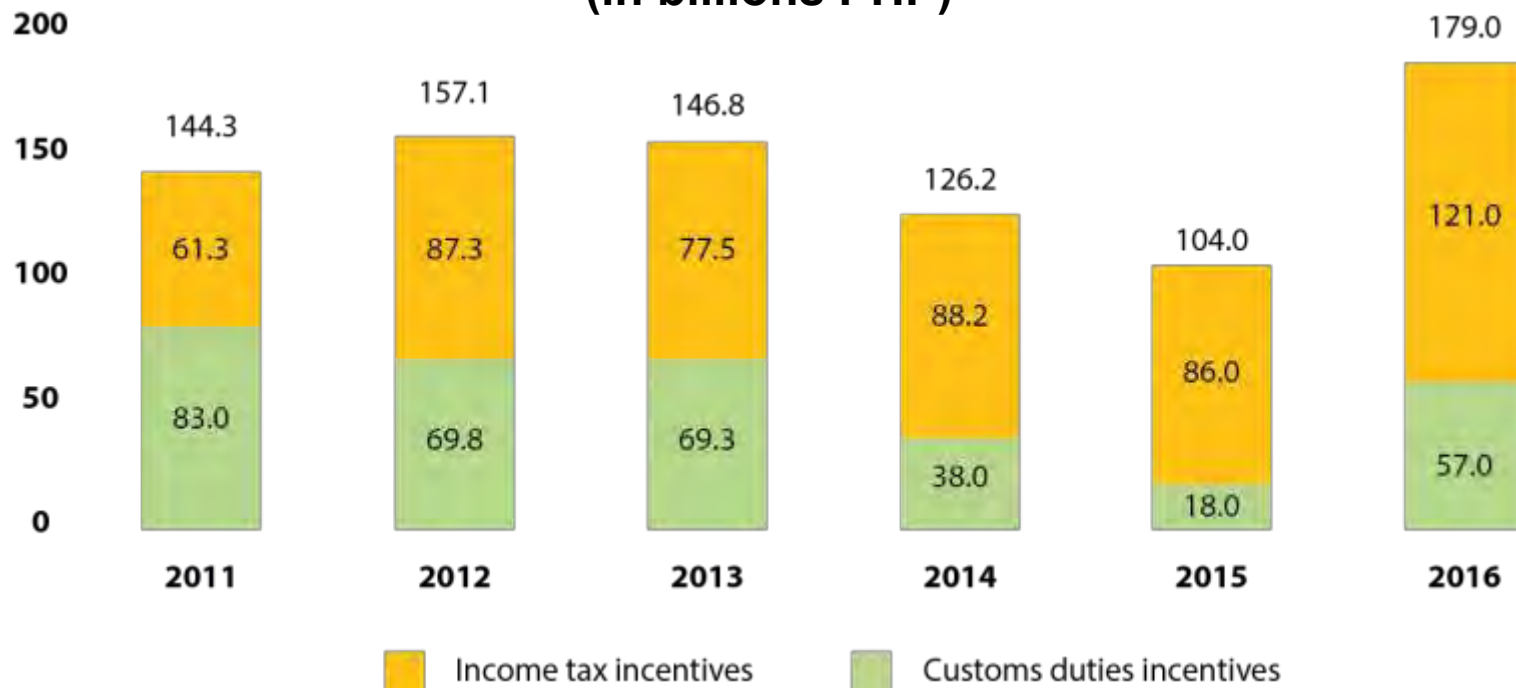
Tax incentives in billion pesos

Type of tax	2015	2016
Income tax	86	121
Customs duties	18	57
Subtotal	104	179
Import VAT (gross)	160	TBD
Local VAT (gross)	37	TBD
Local business tax	TBD	TBD
Subtotal for incentives	301	TBD
Leakage	43	TBD
Total	344	TBD
No. of recipients	2,844	3,102

Source: TIMTA, DOF estimates

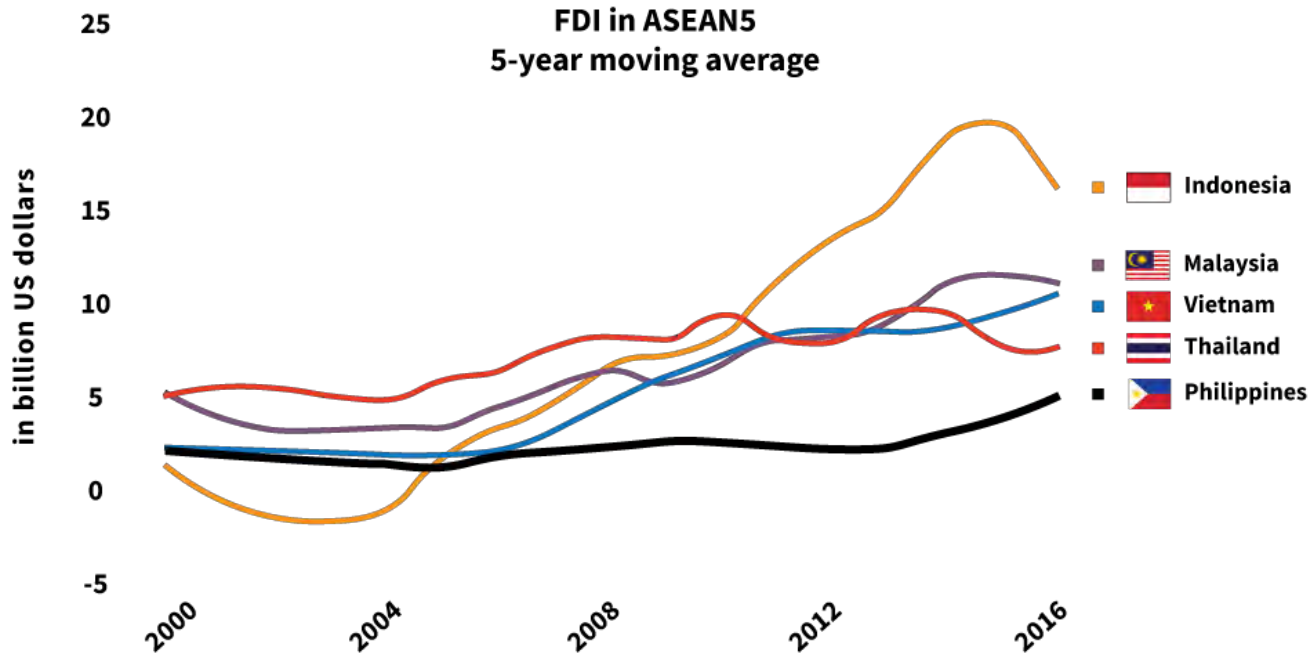
Estimates of tax incentives: income and duties

(in billions PHP)



Source: TIMTA

Despite giving the most generous and forever incentives...



FDI pales in comparison to our neighbors.

Despite giving the most generous and forever incentives...



Source: PSA, UNCTAD, DOF calculations

Export competitiveness has been in decline.

Domestic industries have weak linkages to export industry.

Reliance on imported parts, thus weak domestic content.

Tax incentives usually violate the principles of:



Efficiency



Equity



Simplicity

However, incentives may be justified if they provide net benefit to society as a whole.

Incentives may be important to encourage investments that promote growth and jobs...

...but, investment tax incentives are **tax expenditures** that someone else has to pay.
It is not free money from heaven.



Government needs to ensure efficiency in spending.

(How much tax incentive can we afford?)



Some incentives are unnecessary, i.e., investment would have happened anyway even without the incentives (e.g., available market, quality labor, land, resources, etc.).

Some incentives may be needed to attract investments that support our growth objectives.



Create more
and
better jobs



Promote research
and development



Encourage
innovation



Stimulate domestic
industries



Diversify product space
(e.g., to higher value
exports)

However, they must be **performance-based**, **targeted**, **time-bound**, and **transparent**.

The current incentives system has a big room for improvement.

- Complexity and inequity
Lack of monitoring and evaluation, accountability, and transparency
Incentives as band-aid solution to compensate for past structural weaknesses

It is time that we revisit our incentives system to ensure that we gain from every peso that we grant.



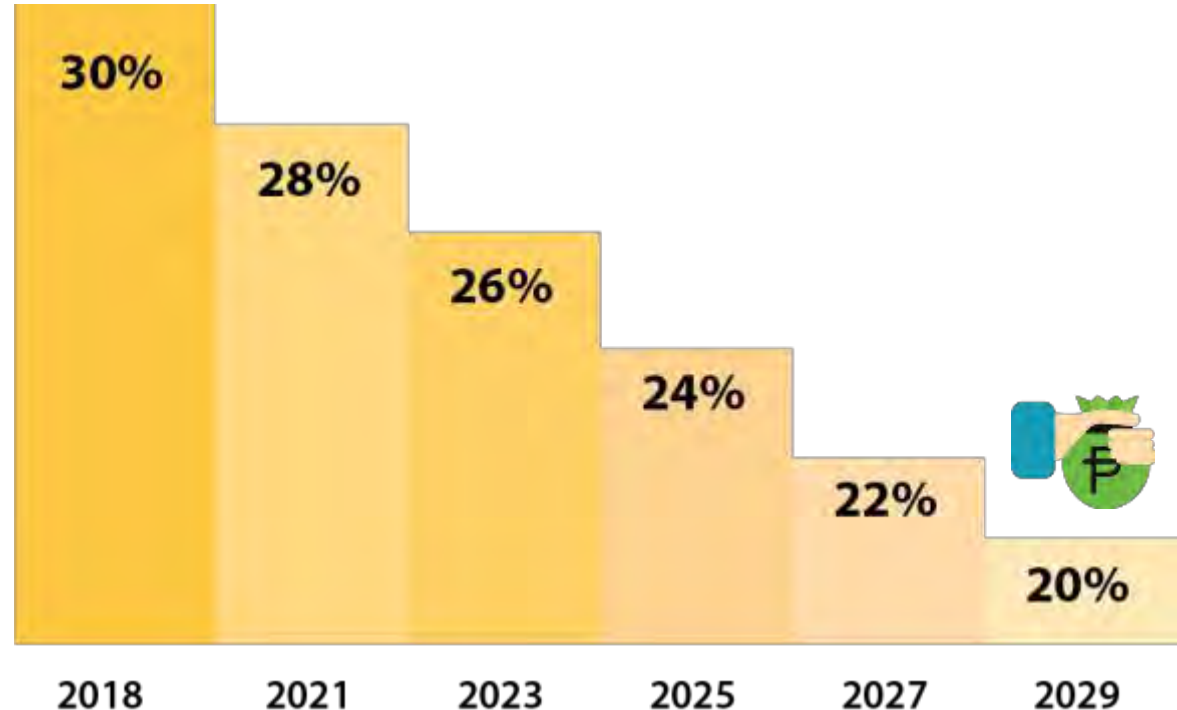


TRABAHO Bill

**Tax Reform for Attracting Better and
High-quality Opportunities bill
(HB 8083)**

Lower corporate income tax

The President may advance the scheduled reduction in the CIT rate when **adequate savings** are realized from the rationalization of fiscal incentives.



Incentives menu – 5 to 7 years

Income tax holiday

Up to 3 years plus 1 year extension if investing in agribusiness, or in less developed areas, or if relocating outside Metro Manila and adjacent urban areas

Special rate (2019)

18% on net taxable income after ITH for up to 5 years including the ITH

- 1.5% to province
- 1.5% to municipality

Year	Special rate (%)	National government (%)	Province (%)	Municipality (%)
2019	18	15	1.5	1.5
2021	17	14	1.5	1.5
2023	16	13	1.5	1.5
2025	15	12	1.5	1.5
2027	14	11	1.5	1.5
2029	13	10	1.5	1.5

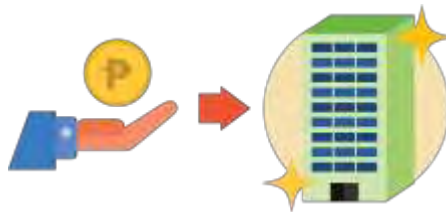
Rationalize investment tax incentives



One menu of incentives applicable to IPAs



No double registration of activities



Only new investment/activities shall be granted income tax incentives



Expansions can avail only of **exemption from customs duty of capital equipment**



Special VAT incentives for exporters: **90% of export sales** are actually shipped out of the country



Domestic firms allowed if included in the **strategic investment priority plan**



Two-year additional incentives for firms moving out of Manila and adjacent areas



Two years additional incentives for lagging regions, conflict, and calamity-stricken regions



Two years additional incentives for agribusiness projects of registered enterprises located outside Metro Manila and urban areas

Incentives menu

- **Depreciation allowance of qualified capital expenditure:**
 - 10% for buildings
 - 20% for machineries
- **Additional deduction of up to:**
 - 100% for research and development (R&D) and training
 - 50% for labor expense
 - 100% for country-wide infrastructure development
 - 50% for reinvestment allowance to manufacturing industry
 - 50% for domestic input expense
- **Enhanced net operating loss carry-over (NOLCO) (5 years)**
- **Exemption from customs duty on imported capital equipment and raw materials**



Incentives menu

- **VAT incentives to registered enterprises whose export meet the 90% of sales threshold, and are within an ecozone or free port:**
 - VAT exemption on importation
 - VAT zero rating on domestic purchases
- **Additional 2 years of incentives for:**
 - registered activities relocating outside Metro Manila and selected urbanized areas adjacent to Metro Manila
 - agribusiness projects of registered enterprises located outside Metro Manila and urban areas
 - projects located in less developed areas or those recovering from armed conflict or a major disaster



Sunset provision for existing incentives

For RBEs which availed of ITH:
Continue until remaining period ends or for a period of 5 years, whichever comes first

For RBEs enjoying existing 5% GIE:

No. of years enjoying 5% GIE	No. of years allowed to continue
5 years below	5
5 to 10 years	3
Above 10 years	2

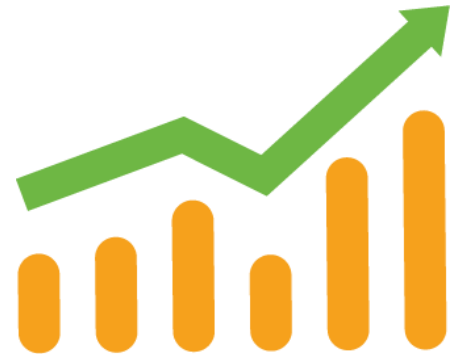
Others (SIPP)

A 3-year SIPP shall be formulated by BOI and approved by the President.

- BOI shall ensure that the more targeted list includes activities with significant positive externalities
Only the President may propose activities or projects not in the SIPP that may be granted tax incentives

Integrate tax expenditure reporting into the budget process.

- Incentives will not be budgeted but should be reported as a tax expenditure for transparency purposes



Earmarking provisions



- **Structural adjustment fund to compensate workers that may be affected due to rationalization of fiscal incentives:**
 - P 500 million for targeted cash grants
 - P 500 million for targeted trainings
 - P 5 billion for skills upgrading of IT-BPO workers
 - P 15 billion for development of infrastructure and economic activities in areas around IPAs
- **Earmarking for student vouchers, housing vouchers, and universal healthcare**

Incentives must be



Performance-based



Targeted



Transparent



Time-bound

With effective **monitoring and evaluation** system
and anchored on a **strategic investment priority plan** that emphasizes:



Job creation



**Research &
development**



**Countryside
development**



Skills training



Innovation

Thank you!



PRESIDENT RODRIGO ROA DUTERTE
STATE OF THE NATION ADDRESS 2018

"I am committed to a comprehensive tax reform and I ask the Congress to continue the job. I hope to sign Package 2 before the year ends.

I urge the Congress to pass it in a form that satisfies our goals and serves the interests of many, not just the wealthy few."



For more information, please visit:



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dof.gov.ph/taxreform

For questions, you may directly email us at:

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